STATE OF CALIFORNIA GRAY DAVIS, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

April 30, 2003 **Agenda ID # 2160**

TO: PARTIES OF RECORD IN INVESTIGATION 97-07-018

This is the proposed decision of Administrative Law Judge (ALJ) Ryerson. It will not appear on the Commission's agenda at the next regular meeting 30 days after the above date. The Commission may act then, or it may postpone action until later.

When the Commission acts on the proposed decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

The proposed decision of the ALJ was mailed to the parties in accordance with Public Utilities Code Section 311(d) and opportunity for comment was provided pursuant to Rules 77.2-77.5 of the Rules of Practice and Procedure. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service. Comments should also be electronically mailed to me at ang@cpuc.ca.gov.

/s/ Angela K. Minkin
Angela K. Minkin, Chief
Administrative Law Judge

ANG:avs

Attachment

Decision **PROPOSED DECISION OF ALJ RYERSON (Mailed 4/30/2003)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's own motion into the operations, practices, rates and charges of the Hillview Water Company, Inc., a corporation, and Roger L. Forrester, the principal shareholder and president, Respondents.	Investigation 97-07-018 (Filed July 16, 1997)

Carol A. Dumond, Attorney at Law, and Mohsen Kazamzadeh, for the Commission's Water Division.
Douglas W. Stern and Leslie Ravestein, Attorneys at Law, and Roger L. Forrester, for Hillview Water Company, Inc., and Roger L. Forrester, respondents.

FINAL OPINION

TABLE OF CONTENTS

TITLE **PAGE**

FINAL OPINION

Summary

This decision resolves all of the outstanding issues that relate to the above-captioned Order Instituting Investigation (OII). These issues relate to the respondents' alleged violation of statutes administered by the Commission, as well as Commission Rule of Practice and Procedure (Rule) 1.[1] We determine that the respondents, Hillview Water Company, Inc. (Hillview or the company) and Roger L. Forrester (Forrester), violated Section 491 and Section 825 of the California Public Utilities Code, and we order the respondents to prepare a reconciliation of accounts for the period from January 1, 1991, to and including July 31, 1998. We also provide that the proceeding may be reopened for the limited purpose of adjusting Hillview's rates if the reconciliation indicates that the company's revenue requirement is materially inaccurate, and we establish a five-year probationary period to prevent a recurrence of these violations. Investigation (I.) 97-07-018 is closed.

Introduction and Procedural History

Hillview is an investor-owned water company serving rural areas in and around the community of Oakhurst in Madera County with approximately 1,370 customers, and thus designated a Class C water utility. Hillview was first organized in 1961, and was incorporated in 1978, giving the company a separate corporate existence from its owners. Respondent Forrester is currently a 50.5% equity holder; his sister is the holder of the remaining 49.5% equity interest.

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[1] Ancillary issues concerning rates and service that were at one time incorporated in this proceeding under Ordering Paragraph (OP) 7 of the OII were separately addressed in interim decisions issued earlier in this proceeding.

Forrester and his sister received ownership of the company in December 1981 from their father, Linton Forrester (Linton). At that time respondent Forrester, who had previously been a hospital administrator for 18 years, also assumed responsibility for managing the company. He testified that he has been president of the corporation since 1983, and that he had no training in managing a water company before he began managing Hillview. For some time, Judith Forrester (Judith), now his ex-wife, assisted with office responsibilities for the company.

In 1984, Hillview interconnected four of its service areas to create a single operating system. We also combined all of Hillview's districts for ratemaking purposes in that year. (Decision (D.) 84-11-089 (November 21, 1984).) Consequently, all of its accounts after that date reflect the system as a whole.

At some point in the early 1990s, Forrester began to experience domestic difficulties with Judith, ultimately resulting in the couple's divorce. (*See* Transcript (Tr.) 1055: 1-7.) The associated problems appear to account for a number of material bookkeeping omissions relating to a Safe Drinking Water Bond Act (SDWBA) loan, as well as the handling of a shareholder loan transaction discussed in detail below. These events contributed to our decision to institute this investigation.

Hillview did not utilize accounting or legal professionals in its operations until 1996. At that time, Hillview first engaged the services of Matt A. Peasley (Peasley), a Certified Public Accountant with small utility regulatory accounting experience, to perform a review of its 1994 and 1995 financial statements. Hillview has continued to retain Peasley to provide accounting services, and also utilizes regulatory legal counsel.

Starting in 1994, and continuing until 1996, irregularities in the company's regulatory compliance came to the attention of the Commission's Water Division (WD) through customer complaints. Following an audit and review of Hillview's operations, the WD asked the Commission's Consumer Services Division (Staff) to pursue formal enforcement action.[2] In response to Staff's request, we issued this OII to determine whether the respondents had violated Sections 491, 581, or 825 of the California Public Utilities Code,[3] or Rule 1.

Staff alleges that Hillview and/or Forrester had, prior to the July 16, 1997, the date of the OII's issuance, committed the following acts contrary to these statutory and regulatory strictures:

1. Violated Commission orders on extension of service to new customers;
2. Submitted falsified contracts or information in response to a request from the Commission;
3. Required customers to pay unauthorized fees for the connection of service and in turn rebated amounts in contravention of tariff and service extension requirements to shopping center developers;
4. Diverted revenue collected expressly to repay a SDWBA loan from a special account, and applied the funds to other purposes, including personal business use by Forrester;
5. Submitted Advice Letter (AL) 53 for additional authority to expand facilities and increase indebtedness, and in it misstated the level of the special fund account due to

[2] Because several staff organizational changes occurred both before and after the institution of this proceeding, we collectively refer to all Commission enforcement staff personnel as "Staff" throughout this decision.

[3] All statutory references are to this Code unless otherwise indicated.

diversion of funds in a manner prohibited by Commission rules or orders;

6. Overstated long-term debt and Hillview's plant account by showing loans secured by Forrester for personal business as utility purpose indebtedness and for expenditure on plant used by Hillview; and
7. Secured a personal loan of $350,000 from a developer, then asked the Commission for authority to repay it without acknowledging that the loan was used, or intended for use, for a personal or non-utility purpose.

The OII "initiate[d] an investigatory proceeding and place[d] the [r]espondents on notice" of the alleged violations, and contemplated that we would impose sanctions, order refunds, and establish a reduced revenue requirement and adjusted rates in the event that customers were overcharged because of the use of an excessive revenue requirement to set Hillview's rates. (OII, pp. 2, 4.) We directed Staff to serve a copy of its audit or investigatory report on the respondents and any other interested parties not later than 10 days before a prehearing conference (PHC), which we directed to be held before an administrative law judge (ALJ). (OII, p. 4.)

The OII noted that we were aware the California Department of Justice was concurrently investigating whether the same conduct alleged in the OII constituted possible criminal behavior. (OII, p. 2.) Before we issued the OII, the Attorney General had seized investigative materials from our San Francisco and Los Angeles offices for this purpose pursuant to a search warrant. The criminal investigation was in progress for more than two years, but was ultimately discontinued. While in progress, however, essential documents and records were effectively unavailable to the parties, and the ALJ held our investigation in

abeyance after the respondents requested a stay until the documents were released.[4]

Staff issued the investigatory (or audit) report November 20, 1997.[5] On December 4, 1997, the ALJ conducted the initial PHC, one of several concerning the resolution of the enforcement issues raised in the OII.[6]

The parties attempted to negotiate a resolution of the issues under investigation, and on April 17, 2001, Staff and the respondents jointly filed a motion asking us to adopt a settlement agreement to conclude this proceeding. In D.02-01-041 (January 9, 2002), we concluded that the proposed settlement did not satisfy our criteria for adoption, and encouraged the parties to renegotiate certain features to address our concerns. The parties were unable to do so, however, and the investigation progressed to a formal evidentiary hearing (EH) following discovery. In a Ruling issued September 10, 2002, the ALJ identified the issues summarized above as those on which he would receive evidence at the EH. He also rejected consideration of certain issues proposed by Staff that were beyond the scope of the OII, including those relating to events that allegedly occurred after the OII was issued.

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[4] On April 25, 2000, the ALJ issued a ruling resuming our investigation upon receiving written confirmation that the criminal investigation was closed.

[5] In addition to serving the respondents, Staff apparently disseminated this report to aggrieved Hillview customers at or before the initial PHC.

[6] OP 7 of the OII required any proposal to increase rates or charges, as well as any individual complaints filed against Hillview, to be consolidated with the enforcement proceeding until further notice. Other PHCs were separately conducted in connection with those ancillary matters throughout the course of this proceeding, and the underlying issues were resolved in interim decisions.

A six-day EH began on October 21, 2002, and concluded on December 19. The parties filed briefs in accordance with a briefing schedule established at the conclusion of the EH, and the proceeding was submitted on January 31, 2003.

Background

The allegations of regulatory noncompliance that caused us to institute this investigation fall into two general areas of Hillview's operations. The first area is the company's borrowing and lending activities, particularly where indebtedness was incurred without specific prior Commission approval. Our concern, and that of the statutes we enforce, is that we must be in a position to prevent potential harm to the utility's customers from unjustifiable rates or degradation of service quality as a consequence of improvident borrowing. The second area is that of the company's handling of advances and fees from developers and individuals for extending and increasing the company's facilities to meet the needs of new customers. Our concern here is with preventing the exaction of unauthorized fees and charges from these customers, resulting in unjust enrichment of the company and its owners. The facts that Staff brought to our attention about these two areas of Hillview's activities prompted our concern, and our decision to examine them more closely in this formal proceeding.

1. Hillview's Borrowing and Lending History

Several loan transactions, some of them interrelated with others, are the subject of this investigation. To make the regulatory compliance issues they pose understandable, we must recount a good deal of Hillview's borrowing history.

In 1980 we authorized Hillview to obtain a loan from the California Department of Water Resources (DWR) under the SDWBA. (D.91560 (April 15, 1980).) Our decision required Hillview to establish a surcharge for each service area to provide a means for repaying the loan. Hillview deposited

the proceeds of the SDWBA loan surcharge in a special account maintained with Golden Oak Bank during the period pertinent to this proceeding. In 1987, we authorized Hillview to increase the borrowing from DWR by $262,283. (D.87-09-029, as modified by D.87-11-051.) Hillview used the same Golden Oak Bank account in connection with this new borrowing, and all customer surcharges continued to be deposited into this account.

As disclosed in the course of our Staff audit, between 1980 and 1994, 14 withdrawals totaling $141,516.61were made from this account without Commission approval, for reasons other than repaying the SDWBA loan. Seven withdrawals were made for rollovers of certificates of deposit in which Hillview had invested funds in order to obtain a higher interest rate. Hillview could not support or explain one withdrawal in the amount of $190 made on June 30, 1982. Another, in the amount of $350, was made on May 31, 1992, to correct a deposit error, according to Hillview.

One withdrawal of $25,000 was made on January 31, 1992, to be used for Hillview's general expenses. Hillview admits that we did not approve this withdrawal, but the company sought DWR's prior approval and received an affirmative response from DWR in a letter dated January 27, 1992. (Exhibit (Exh. 129.)[7]

The remaining four withdrawals were made, respectively, on June 30, July 31, September 30, and October 30, 1993. The first was in the amount of $2,220.17; each of the others was in the amount of $4,440.33. Forrester testified

[7] Exhibit Numbers refer to the exhibits marked and received at the EH that commenced October 21, 2002 and concluded on December 19, 2002, and each exhibit is so identified

Footnote continued on next page

that the purpose of these withdrawals was to "make payment on the $350,000 obligation of Hillview" to Judith and himself. (Exh. 82A, pp. 16-17.) This obligation arose from a loan that the company had made to the Forresters shortly before, as explained in greater detail below.

Forrester concedes that none of these withdrawals was made with prior Commission approval. He testified that Judith withdrew the money on each occasion without his knowledge. As an officer of the company who handled office duties before her relationships with Hillview and Forrester ended, she was apparently in a position to do so. The respondents offer no specific evidence to indicate when the Forresters began to experience marital problems, but the timing of these withdrawals coincided with the approximate period Forrester indicated their marital breakdown occurred.

The $350,000 personal loan to which this testimony refers is part of a second transaction that aroused our concern when it came to light in the Staff audit. The structure of this transaction is somewhat intricate, and subsequent refinancings further complicate our ability to trace its history. Essentially, the chronology of relevant events began in April 1991, when Hillview needed funds to build two water treatment plants. Forrester testified that Hillview's credit at the time made it unlikely that the company would be able to obtain a commercial loan on favorable terms. However, Hillview had what Forrester characterizes as a "long history" of dealing with the individuals involved in 41/49 Highway Junction Projects, Limited (41/49), a commercial real estate developer in Oakhurst, and proposed to borrow the funds from that entity. Although

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on the exhibit stamp. These exhibits should not be confused with similarly numbered exhibits received during hearings in other phases of this proceeding on earlier dates.

unwilling to loan funds to Hillview, 41/49 was willing to make a personal loan of $350,000 to Forrester and Judith, secured by the couple's real and personal property. Forrester testified that his intention was in turn to lend the $350,000 to Hillview, and that he did not believe at the time that Commission approval was necessary in order to do so.

On June 5, 1991, the Forresters entered into a formal written loan agreement with 41/49. (Exh. 24.) The loan was secured by 500 shares of Hillview stock, and by a deed of trust recorded against title to real property owned by the couple. As part of the consideration for the loan, Forrester agreed that Hillview would issue a letter to the County of Madera, stating that 41/49 had no further obligation to provide supply and storage for certain commercial developments in Oakhurst. Forrester testified that he did not know 41/49's purpose in requesting this letter as part of the transaction. The Forresters received the loan proceeds in two equal payments of $175,000, the first upon signing on June 5, 1991, and the second on June 5, 1992.

Between June 30, 1991, and the end of December 1992 the Forresters loaned Hillview $160,553.03, interest-free. Forrester testified that this obligation of Hillview is evidenced by cancelled checks, journal entries, and bank statements, which were collectively received as Exh. 113A. He further testified that Hillview used these funds to build plant.

The Forresters' expenditure of these funds constituted part of the basis of a subsequent transaction, in which Hillview nominally loaned $350,000 back to the Forresters, that was recorded by Hillview as of December 31, 1992. This transaction was structured as follows. First, the Forresters forgave the $160,553.03 owed to them for the previous six months' expenditures, canceling that debt. Second, the Forresters assumed an unpaid $47,900 loan obligation

arising from a loan that Linton, Forrester's father, had made to the company at a much earlier time, canceling that debt also. Third, Hillview would receive a note from the Forresters in the amount of $141,546.97. The total of these three figures is $350,000, the amount of the loan. There is no indication in the record that a cash disbursement of $141,546.97 was ever made to the Forresters in satisfaction of this note, and the only indication that the Forresters ever received any cash relating to this loan from Hillview is the evidence that Judith made four withdrawals totaling $15,541.16 between June 30 and October 30, 1993.

Hillview's 1992 Annual Report to the Commission, filed with the WD on March 6, 1993, reports this transaction as part of the company's long term debt, specifically as a "loan *from* individual" with a 12% interest rate and a 14-year term, incurred on June 7, 1992. (Exh. 26, p. 3, italics supplied.)[8] Forrester admits that this entry is erroneous. He testified that the error occurred because the transaction was incorrectly recorded on Hillview's books, specifically by inadvertently being combined with another entry.

Notwithstanding the absence of evidence that the Forresters ever received all of the $141,546.97 they purportedly borrowed from the company in this transaction, Forrester testified that he paid off the full amount of the note in the first seven months of 1998. (Exh. 82A, p. 24.) The details of this reimbursement are set forth in Exh. 118, a compilation prepared by Peasley from Hillview's records to comply with the provisions of a loan agreement with

[8] The promissory note was actually signed by Forrester on behalf of Hillview on June 5, 1992. (*See* Exh. 117.)

another lender in a more recent refinancing.[9] This document reflects that there were intervening transactions (discussed below) with respect to the original loan back to Forrester, because the repayment otherwise is not consistent with the record of funds received by the Forresters, or with the names shown for the borrowers reflected in Exh. 118.

[9] This compilation is not audited, and is based solely upon the representations of Hillview's management.

Note 2 of the compilation reports that on January 31, 1998, Jacqueline Forrester (Jacqueline), who was by then Forrester's wife by remarriage following the dissolution of his marriage to Judith, agreed to apply the balance of a series of notes due her from Hillview, plus accrued interest, toward repayment of the $141,547 (a rounded figure). These notes reflected various amounts she had loaned to the company between April 9, 1997, and January 16, 1998, totaling $85,017. The remaining repayments reported in the compilation were in the form of a transfer of office furniture and equipment with a value of $4,288 from Jacqueline to the company on January 31, 1998; a cash payment of $40,000 on May 15, 1998; and another cash payment of $12,242 on July 7, 1998. Note 4 explains that the latter sum was part of a cash payment of $28,997 received from Forrester and Jacqueline, and that the remaining $16,755 was applied against a current cash receivable due to Hillview from Forrester alone.

The intervening transactions occurring between the loan to the Forresters recorded on December 31, 1992, and the apparent payoff of the remaining balance of that loan in 1998, are a series of refinancings that were accomplished in and after 1994. Forrester testified that in that year Hillview refinanced its $350,000 obligation to Forrester and Judith by obtaining a loan from the United States Small Business Administration (SBA) through Golden Oak Bank in the amount of $424,000. Forrester admits that he did not obtain Commission approval for this loan, because he was "focused on Hillview's needs and [his] personal problems with [his] ex-wife." (Exh. 82A, p. 25.)

Hillview's unauthorized borrowing had come to our attention by the time we granted Hillview's August 2, 1993 request for a general rate increase. In Resolution (Res.) No. W-3833, issued March 9, 1994, we noted that Hillview had

incurred long-term debt without Commission authorization as required by Section 816, and that the company should request authorization for the debt it had incurred as soon as possible. The Commission awarded Hillview a rate of return at the low end of the range recommended by Staff in that rate case as a consequence of Hillview's failure to comply with this loan authorization requirement.

Several months later that year, Hillview obtained two new loans from the National Bank of Cooperatives (CoBank). The first, in the amount of $540,000, was obtained to refinance the existing unauthorized commercial debt. The other, in the amount of $960,000, was to be used to refinance the existing SDWBA loan and to pay for approximately $266,650 in improvements. Hillview had sought prior approval of this transaction from the Commission by filing a draft AL on October 6, 1993. We granted the request on November 22, 1994, in Res. No. F-632, which noted that Hillview was in violation of Section 825 for failing to secure prior approval of the commercial debt, citing three Golden Oak Bank loans and one from General Motors Acceptance Corporation. We also granted authority for the company to apply the SDWBA reserve, and any remaining surcharge overcollection relating to the SDWBA loan, to reduce the amount of the $960,000 CoBank loan.

Using the proceeds of the CoBank loan, Hillview repaid the SDWBA loan. However, in Res. No. F-644 (March 13, 1996) we granted Hillview authority to use $112,000 of the remaining SDWBA loan reserve and surcharge overcollection to finance the construction of certain new facilities, rather than paying down the CoBank loan. We did so to enable Hillview to avoid additional borrowing that would otherwise have been necessary to finance these improvements. Staff claims that Hillview understated the balance remaining in

the surplus account by $135,812 after repaying the SDWBA loan, and that as a consequence, Res. No. F-644 granted Hillview authority to borrow more funds than necessary from CoBank. Staff contends that this resulted in overstatement of the company's rate base, producing higher rates for customers.

2. Fees for Facility Additions

Hillview's history is closely associated with the development of real property by builders and developers in the rural territory it serves, and its facility expansion is interrelated with that property development.[10] In 1985, the company first began charging a "Supply and Storage" fee under the terms of a main extension agreement it executed with the developer of a development known as Indian Springs. Under the agreement the developer would pay Hillview a specified amount for supply and storage for each lot in the development that was connected for service.

Under this arrangement the obligation to pay the fee to Hillview was that of the developer, who in turn passed the fee on to each individual lot purchaser. As a consequence, no individual purchaser made a payment of this fee directly to Hillview. Hillview says it agreed to this arrangement, under which the developer paid the fee on a per-lot basis at the time each service connection was made, rather than all at once when it commenced development

[10] The pace of Hillview's facility expansion in the past two decades accelerated until we found it necessary to impose a moratorium on new service pending the addition of supply and the provision of certain required treatment facilities. Financing and construction of these improvements were delayed until recently because of the cloud over Hillview's financial circumstances that resulted from the other issues raised in this investigation. Those issues were resolved in other phases of this proceeding, as required by OP 7 of the OII.

of the entire parcel, for two reasons. First, it spared the developer from having to commit costly capital to the payment of fees that it might not be able to recover

for many years. Second, Hillview did not anticipate that the supply and storage facilities to be financed with these fees would be needed until the development grew to a certain size, so the company did not need to collect the funds immediately in Forrester's judgment.

Over time this practice was converted to a third-party beneficiary arrangement under which the lot purchasers each paid a per-lot share of the total directly to Hillview, in contrast to the previous practice, under which the developer collected the fee from each new purchaser and remitted it to Hillview. This fee was paid on behalf of the developer at the time a lot owner desired the service, and Hillview agreed to accept payment in this manner. In addition to supply and storage fees, fees for main extensions (to the extent that they were the responsibility of the developer) also were handled in this manner.

The form of written main extension agreement Hillview used to establish these obligations was one of several forms approved by the Commission to implement tariff rules. Hillview modified one version of this form by inserting a provision concerning payment of the supply and storage fee, a term that is not used in any applicable tariff. Forrester testified that the company used the term interchangeably with "special facilities fee," a tariff term. Hillview ceased to use "supply and storage fee" after the practice came under criticism by Staff.

Forrester testified that the specific method of payment of these fees depended upon the circumstances of the developer or the particular development. Payment of main extension fees was required from a developer either initially upon execution of a main extension agreement, or on a per-lot basis. A developer that negotiated a per-lot supply and storage fee in its main extension agreement either had to pay a proportional fee directly to Hillview

upon connection of water service to a lot, or out of escrow from the developer's proceeds upon sale of the lot. Forrester testified that the selection of the method was left to negotiation between the developer and the lot purchaser.

Forrester testified that he now understands that, following revision of the applicable tariff in 1982 and until at least 1993, supply and storage fees were permitted to be collected only from developers. At the time of these events, on the other hand, he believed it was permissible to accept payment of these fees from individual lot purchasers on behalf of the developer. All of these fees were recorded as Contributions in Aid of Construction (CIAC) and were used to construct supply and storage facilities. They were not included in Hillview's rate base, with the consequence that the company has not earned any return on them, and customers other than those within the affected developments did not pay for the facilities. (Exh. 87A, p. 10.)

The procedure Hillview followed for recording supply and storage fees was to list in its Supply and Storage Fee Account Passbook (Exh. 217) the name of the person for whose lot the fee was paid, the lot number, the date, and the amount paid. The funds were then deposited into the Supply and Storage Fee account. (Exh. 87A, p. 10.) Notwithstanding the existence of these records, the parties have not been able to compile a reliable list of all such fees collected that could be used to refund amounts Staff claims are due under tariff requirements. As nearly as we can determine, this is because the way in which the receipt of some of the fees was recorded may not have accurately reflected their purpose, and because the fractionated manner of collecting these fees on individual lots rather than entire development parcels, coupled with the subsequent resale of

some of the lots, make them impossible to trace. Even when the respondents were working cooperatively with several members of our Staff over a lengthy period to develop an accurate list as part of their settlement efforts, they were unable to do so. The best list they could compile (Exh. 102) indicated in many instances that proof of payment of the fee was missing, and would have to be furnished by claimants if Hillview became obligated to refund the fees under the terms of the settlement.

In 1993, Staff performed a limited audit of Hillview, and examined the company's CIAC account as part of that audit. In their Report on Audit, dated June 25, 1993 (Exh. 105), the auditors stated:

> Initially, [we] had concerns with some amounts recorded in the CIAC account which Hillview called "Supply and Storage Fees" in [its] contributions contracts and in [its] accounting records. This concern focused on whether these fees should be considered to be contributions under existing tariffs. Further examination revealed that these amounts in fact were for Other Special Facilities as allowed under tariff rule 15 and were appropriately recorded in Hillview's CIAC accounts. After clearing up this concern [we] found Hillview's contributions and advance account balances…to be correct. (*Id.*, p. 3.)

As a result of correspondence from members of our Staff beginning in early 1994, the respondents became aware that WD believed Hillview's direct receipt of supply and storage (or special facilities) fees from any individual customer, under any circumstances, was contrary to Commission-approved tariffs. Accordingly, in June of that year Forrester instructed his staff not to include supply and storage fees in the company's Main Extension Contracts or accept such fees from individuals, and the practice was discontinued.

Discussion

With this factual background we turn to a discussion of the specific issues raised in the OII, in the sequence established by the ALJ's Ruling of September 10, 2002.

1. Did the Respondents Violate Commission Orders on the Extension of Service to New Customers?

The extension of distribution mains from Hillview's basic production and transmission system to serve new customers described in this investigation is governed by the terms of the company's Tariff Rule 15, a standardized water utility tariff approved by the Commission. The material provisions of Tariff Rule 15 in this dispute were included in an approved version of the tariff in effect from 1982 throughout the period subject to investigation. The parties agree on the substance of those provisions, but differ as to their interpretation.

Tariff Rule 15 requires a main extension contract to be executed by the utility and the applicant(s) in advance of the construction work. The Commission has alternative approved versions of this main extension contract to be used for individual customers and for real estate developers and builders. (Tariff Rule 15 defines the latter to include individuals and others who divide a parcel of land into two or more portions, or who engage in the construction and resale of individual structures on a continuing basis. (Paragraph A.3.b.)) The sum paid by an applicant for a main extension is an advance, and is recoverable through refunds paid under a schedule specified in the tariff. An exception is made if, in the opinion of the utility, it appears that a proposed main extension will not, within a reasonable period, develop sufficient revenue to make the extension self-supporting, or if for some other reason it appears to the utility that a main extension contract would place an excessive burden on customers. In this

event the utility may require non-refundable contributions of plant facilities *from the developer in lieu of a main extension contract.* (Paragraph. C.1.d.)

Staff contends that because of the cited language in Paragraph C.1.d above, these tariff requirements must be read in the alternative: Either a special facilities (or supply and storage) fee is refundable under the terms of a main extension contract, or it is a discretionary non-refundable contribution from the developer. Because Forrester testified that Hillview collected the fees pursuant to Paragraph C.1.b, which required them to be refunded as advances, the company's admitted failure to do so violated the refund schedule provided in Paragraph C.2.c.[11]

The respondents argue that refundable advances under main extension contracts and nonrefundable contributions under Paragraph C.1.d are not mutually exclusive. They cite D.02-01-014 (January 9, 2002) in *Application of Del Oro Water Co., Inc., etc.,* in support of their contention that Hillview had the prerogative to receive the sums involved either as refundable advances or as nonrefundable contributions. This may be true, but the evidence is quite clear that if Hillview made this election, it did not do so in the proper manner: If Hillview intended these fees to be nonrefundable contributions, it should not have received them under the terms of a main extension contract, as that is the written instrument under which the refund arrangement is memorialized.

[11] Under Hillview's Tariff Rule 16, the company was generally forbidden from charging individual customers a fee for making new service connections until June 9, 1992, but following that date, as a Class C utility Hillview could lawfully accept from such customers amounts in contribution as connection fees, and amounts in contribution as facilities fees, calculated in accordance with Commission-approved schedules.

Consequently, we agree with Staff that there is substantial evidence of Hillview's violation of Commission-approved tariff procedure in collecting "supply and storage fees" from individuals. Hillview admits violating the tariff, and concedes that it was not proper to alter the approved form of its main extension contract to collect an unauthorized "supply and storage" fee. To complicate matters, Hillview admits that it mistakenly used the wrong form of agreement on a number of occasions, confusing a contract form used for developers with that used for individuals.

The respondents argue, as to any payments regarded as advances, that Paragraph C.1.d does not specify the time or manner of payment, and that per-lot installment payments of special facilities fees was not prohibited by the tariff. They also contend that Tariff Rule 15 did not prohibit the third-party beneficiary arrangement. We do not find these arguments persuasive. Our inability to reconstruct the record of fee payments to determine reliably all of the persons who might have been entitled to a refund is compelling enough evidence that this arrangement did not carry out the purposes of Tariff Rule 15.

Despite these errors, it does not appear that these actions harmed Hillview's customers. All of the sums collected for main extensions and special facilities were properly recorded in its CIAC account, as our auditors found in 1993. The funds in that account were devoted to the construction of facilities in districts with which they were associated, and were not included in its rates. Thus, while Hillview's customers paid for the facilities up front, they did not amortize them over time through higher water rates. Moreover, because the fees were treated as contributions, Hillview has never been able to earn a return on them. Even lot owners who subsequently sold their lots were not harmed under the pay-as-you-go arrangement into which Hilview entered with developers,

because the added value of the fees was reflected in the market value of their properties. Consequently, we will not require Hillview to attempt once again to reconstruct the history of these fees, and we will not impose a fine or penalty, as we would in an instance where the public was harmed.

2. Did the Respondents Submit Falsified Contracts or Information to the Commission?

The allegation that the respondents furnished falsified documents to the Commission in response to a request relates to an incident that occurred in the course of our auditor's 1996 investigation. In a data request the auditor asked for lists of Hillview's new customers from 1993 and 1995. The response for this request was due in seven days.

Instead of responding with a list of these customers, Hillview responded by submitting photocopies of these customers' application forms. The lower portions of the forms were covered with a form of different appearance that had blanks for recording fee payments. Although these documents collectively comprised the customer lists requested by the auditor, Staff alleges that Hillview covered the lower portion of the forms when copying them in an effort to hide information and mislead the Commission.

Jacqueline, who by the time of these events was Hillview's office manager, credibly explained this incident in her testimony at the EH of May 20, 2000, in this proceeding.[12] Essentially, she explained that the forms were copied and produced in lieu of creating a computer-generated list, because Hillview's computer system at the time did not have the capability to do so, and

[12] Jacqueline Forrester died after giving this testimony, and the transcript of her explanation was received as Exh. 83 in addition to being part of the official transcript herein.

because of the short deadline given by the auditor. The bottoms of the forms were covered to prevent confusion, as the company had adopted a second, different form, and the information recorded thereon was not required in order to respond to the data request. Staff accepted Jacqueline's explanation at the earlier EH, and it is credible. There is no new information in the record that would cause us to doubt Staff's earlier determination. We find that, although the lower portions of application forms were admittedly covered for photocopying, this fact did not represent a deliberate effort to mislead the Commission, nor did it hinder Staff's investigation.

3. Did the Respondents Charge Customers Unauthorized Fees for the Connection of Service and in Turn Rebate Amounts in Contravention of Tariff and Service Extension Requirements to Shopping Center Developers?

Staff alleges that in 1991 the respondents entered into an arrangement whereby Hillview would assist 41/49, the developer of the Old Mill Village commercial development, by getting Hillview customers to reimburse 41/49 for its special facilities fees. The customers to which this allegation relates were Longs Drugs and Vons Market, each of which built retail facilities on lots in the development. As set out in Staff's audit report, which constitutes its only evidence in support of this contention,

> When 41/49 completed construction of a building in a shopping center and the building was ready for occupancy, 41/49 advised the store, market, or other retailer that was going to occupy the building that supply and storage fees would have to be paid to [Hillview] in order for it to have water service. When the store, market, or other occupant paid the money…[Hillview] immediately turned the money over to 41/49. (Exh. 68, p. 27.)

There is no controversy that in concept this is a correct rendition of the procedure that was followed. Staff admits that this produced no direct benefit to

Hillview, but claims that it benefited 41/49 by making its properties appear less expensive and thus more attractive, and also benefited Forrester and Judith, by constituting part of the consideration for the $350,000 loan they received from 41/49.

The respondents explain that 41/49 had already paid plant and special facilities fees up front for Old Mill Village, and that the amounts returned to 41/49 were simply refunds of advances under the main extension agreement. The respondents also admit that they should have entered into main extension contracts with Longs and Vons under Paragraph C.2.d, and that this was not properly accomplished.

The $350,000 loan transaction between 41/49 and the Forresters is explained in detail above. There is no evidence in the record that this was a *quid pro quo* arrangement, and Forrester denies that it was, because 41/49 had already fulfilled its obligation to pay these fees. Although we are concerned about the closeness of the relationship and informality of the business dealings between 41/49 and the respondents, which aroused suspicion when they came to light during Staff's investigation, Staff concedes that Hillview's customers suffered no harm as the result of Hillview making these refunds.

Hillview admits that it did not carry out the refund transaction in accordance with Tariff Rule 15, but our inquiry must end there. Any contention by Staff that the payments were "illegal" or part of an "unlawful scheme" are either unsupported by the record or beyond the enforcement jurisdiction of the Commission.[13] We will not impose any penalty in relation to this allegation.

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[13] As explained in our Introduction above, all of these contentions were investigated by the California Attorney General with Staff's cooperation. That investigation was

Footnote continued on next page

4. Did the Respondents Divert Revenue Collected Expressly to Repay a SDWBA Loan from a Special Account and Apply the Funds to Other Purposes, Including Personal Business Use by Forrester?

Staff notes that Res. No. F-632 authorized the respondents to enter into the CoBank loan contracts for $540,000 and $960,000 for the specific purpose of refinancing existing unauthorized commercial debts, namely the SDWBA loan and $266,650 in improvements. Staff alleges that some loan proceeds instead were used to pay Forrester's past due property taxes and electric bills, and for some construction activities that had already been reimbursed through surcharges collected from customers.

The underlying facts are explained earlier in this decision. Regarding Hillview's construction activities, Res. No. F-638 (April 26, 1995) authorized Hillview to increase its loan agreement by $100,000 over the amount approved in Res. No. F-632, to reimburse Hillview for funds already spent for facility construction and improvements, and those improvements were made. As to the allegations regarding improper payment of taxes and electric bills, the respondents point out that Forrester personally owns the building in question and leases it to Hillview under the terms of a triple net lease that obligates Hillview, not Forrester, to pay these expenses. (Exh. 74; Tr.881: 9-23.) Hillview's payment of these expenses was therefore entirely proper.

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terminated, and no indictment was sought in Madera County Superior Court. We understand that the investigative documents were then turned over to the United States Internal Revenue Service.

All of the evidence indicates that we examined and approved these transactions before we issued the OII. The respondents have effectively rebutted any showing made by Staff to support its theory, and that showing is weak.[14]

5. Did Hillview's AL 53 Misstate the Level of the Special Fund Account Due to Unlawful Diversions?

As explained above, Hillview filed AL 53, asking the Commission to modify Res. No. F-632 by permitting diversion of $112,463.42 of surplus funds from paying down the CoBank loan to paying for new facilities. We granted this request, with the net effect that Hillview's indebtedness increased by that amount.

Staff contends that the net surplus in the loan account was $281,734 on October 23, 1995, when the respondents filed AL 53, and that the special fund was accordingly understated by $169,271. Staff argues that the present value of this figure at the time of the hearing was $200,467. (Exh. 22A.) The derivation of the claimed understatement remains a mystery. The utilities engineer who prepared Exh. 22A did so on the basis of figures in the auditor's workpapers, and calculated account balances by plugging those figures into a formula that in turn relied upon an unsupported assumption. The workpapers were marked for identification at the hearing, but Staff declined to offer them in evidence. Staff has not carried its burden of proof on this issue. However, we will require appropriate relief if an inconsistency in this account is revealed in the reconciliation to be prepared pursuant to our Order.

[14] We note that Staff has devoted only eight lines of argument to this theory in its Opening Brief. This fact suggests to us that the issue is not as significant as it may have appeared to Staff at the time the audit report was written.

6. Did the Respondents Overstate Long-Term Debt and Hillview's Plant Account by Misrepresenting Loans Obtained by Forrester for Personal Business?

Hillview's history of long-term debt and plant account is largely recounted above. Staff relies solely upon Chapters 7 through 12 of its audit report (Exh. 68) in support of the allegations that there is no documentation for expenditures ostensibly used for utility plant, that the respondents misused corporate assets, and that these circumstances explain why the respondents did not seek Commission approval for the "initial" [SDWBA?] loan.[15]

The Staff auditor prepared Chapters 7 through 12 of the audit report (Exh. 68). He adopted all of this material as his testimony at the EH in lieu of providing prepared testimony (Tr. 447 – 478). He was extensively questioned about this report by respondents' counsel on cross-examination (Tr. 478 – 686; 689 – 790) and recross (Tr. 878 – 890), and much of the report was seriously discredited. Little of his testimony was effectively rehabilitated on redirect. His answers to many questions were incomplete, unresponsive or evasive. At times he also displayed personal animosity toward Forrester, and inappropriately expressed anger toward Hillview's management, attorneys, and accountant. All of these factors call into question the reliability of the portions of Exh. 68 that he sponsored, and we accord them little weight.

The portions of Exh. 68 sponsored by this witness are the heart of the investigative report the OII directed Staff to prepare. Staff issued the original

[15] Staff's Opening Brief devotes a short paragraph of argument to these charges, accusing Hillview's management of a "wholesale breach of trust," and representing a "flagrant flouting of state law and Commission authority," but contains no discussion of any evidence demonstrating that such serious allegations are justified.

report on November 20, 1997, and Exh. 68, an amplification of that report, in August 2002, offering it in substitution of the original as Staff's principal testimony. Yet despite the passage of more than five years since we had issued the OII and Staff had issued the audit report, Chapters 7 through 12 remained untouched in the revised version. By contrast, the respondents made a credible showing on the propriety of its loans and expenditures.

Notwithstanding the absence of substantial evidence to support Staff's broad accusations, several discrete issues relating to this aspect of the OII were raised by the parties and should be addressed. Fortunately, there is sufficient reliable evidence to make findings on these issues. We do so to enable the parties to prepare a final reconciliation of Hillview's accounts, so that its financial condition may be accurately established.

First, with regard to the transaction in which Hillview made a $350,000 loan to Forrester and Judith in 1992, a question arose as to whether the Forresters' assumption of a $47,900 loan to the company from Linton was valid consideration. The original debt derives from Linton's payment of Hillview's utility bills, satisfaction of a judgment against the company, and the deposit of $16,000 in cash to the company's general account. Altogether, Linton advanced a total of $50,000 on the company's behalf, but by December 1982 Hillview had repaid only a small portion of this obligation, and the remaining $47,900 was on Hillview's books until the 1992 transaction. We had occasion to review this obligation as early as January 21, 1982. (D.82-01-105 in Application (A.) 61148; *see also* D.82-12-062 in A.82-06-073 (December 15, 1982).) Forrester provided a credible explanation of its origin, and Staff has not persuaded us that any part of the obligation was invalid.

Second, with respect to the 1992 loan from the Forresters to Hillview, the respondents admit that Forrester should have immediately loaned $141,546.97 in cash to Hillview instead of executing a note. Forrester attributes his failure to do so to unspecified "personal problems." (Respondents' Brief, p. 28.)[16]

Third, Forrester admits that a book entry made in December 1992 that included the $350,000 obligation of the Forresters was improperly recorded, resulting in confusion of the company's accounting. He attributes this to the lack of sophistication of Hillview's bookkeeping staff (including Forrester himself) at the time the transaction was recorded. Peasley discovered the error after he was retained and learned that the accounts related to surcharge-funded utility plant, CoBank loans, income taxes, deferred taxes, and CIAC all needed adjustment before the 1995 financial statements could be prepared.

Peasley testified that Hillview had made an error in recording contributed property conveyed by 41/49, as well as the loan payable by Forrester. The company did not correctly record amounts to CIAC equal to the conveyed property, and actually recorded a slight decrease in CIAC. Hillview's records needed an adjustment of $141,546.97 to increase (credit) CIAC. In the loan transaction, Hillview failed to record a loan due from Forrester of $141,546.97(debit). (Exh. 81.) In sum, the entry related to the $350,000 obligation should have reflected:

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[16] We infer from Forrester's other testimony that this is a reference to the breakdown of his marriage to Judith, and that community property problems may have flowed from this event, impairing Forrester's ability to raise cash at the time. The occurrence of such personal problems does not excuse any failure of regulatory compliance, and we do not condone Forrester's actions in so finding.

- Cancellation of the prior loans of $160,553.03 from the Forresters;
- Assumption of Hillview's debt of $47,900 to Linton;
- A receivable from the Forresters of $141,546.97; and
- A debt payable to Forrester of $350,000.

A separate entry should have been made for plant, reflecting:

- $131,158.36 of utility plant, and
- $131,158.36 CIAC.

(Exh. 81, pp. 2-3, 123, and 124; Respondents' Brief, pp. 22-23.)

The consequence of this mistake was that for the 1994 test year, on the basis of which Hillview's rates prior to 2001 were adopted, CIAC was understated by $141,546.97, and rate base was overstated by the same amount. This circumstance in itself would have resulted in rates that were too high. However, Forrester testified that rate base was actually understated, because the recorded average plant in 1994 was $212,581 higher than the test year average plant. (Exh. 82A, p. 26.) This is corroborated by Jacqueline's testimony at the May 20, 2000, EH. (Exh. 83.)

In the 1993 general rate case, we adopted a reduced rate of return for Hillview because of its unauthorized borrowing activities. As a consequence of the current investigation, which was largely the result of the confusion in Hillview's accounting records, Hillview did not have a general rate case between 1993 and 2000. Hillview's average plant increased significantly over that period, and contributions generally decreased. (Exh. 126.) Hillview argues that it has lost part of the return on its actual rate base because of this, and that its loss has

more than offset the consequences of its accounting error, producing unrealistically low rates.

This argument is predicated on the assumption that the corresponding plant, which was contributed by 41/49, was actually installed. Forrester testified that it was, and corroborated his testimony with Exh. 147, a confirming letter from 41/49. Staff has offered no evidence other than the unsupported testimony of its auditor that the plant was not installed.

Despite Staff's failure to prove much of what is alleged in Chapters 7 through 12 of Exh. 68, the evidence concerning these discrete issues is sufficient to support findings, and to indicate a need for further reconciliation of accounts, as provided in our order.

7. Did the Respondents Obtain a Personal Loan of $350,000 from a Developer, Then Ask the Commission for Authority to Repay it Without Acknowledging that the Loan Was Used, or Intended to be Used, for a Personal or Non-Utility Purpose?

The loan transactions at issue are explained earlier in this decision. Staff's argument is based upon Chapter 8 of its audit report (Exh. 68), which characterizes this succession of loans as a "scheme of layers upon layers of loans…apparently designed to hide the true origin of the [CoBank] loan" for which Hillview sought our approval. (*Id.,* p. 40.) In light of the facts of record set forth above, we find that Staff has misinterpreted the evidence. Staff's rendition of the loan history is as follows:

1. In 1991 Forrester obtained a personal loan of $350,000 from 41/49 in exchange for a letter declaring that 41/49 had provided all the required utility plant.
2. In 1992 Hillview "falsely" recorded the $350,000 as a company loan on its books.

3. In 1993 Hillview obtained the $424,000 SBA loan to pay off the $350,000 personal loan, which was now inaccurately recorded on its books, "apparently in order to mislead the Golden Oak Bank and the Commission."
4. In 1994 Hillview came to the Commission for approval of the loan for $540,000 to use to pay off the SBA loan.

Staff characterizes this "compounding" of loans as an attempt to disguise the origin of the loan. (*Id.*, p. 41.)

Staff's rendition is based upon speculation, and the weight of the evidence indicates that its logic is flawed. First, irrespective of the reason why 41/49 requested, and the respondents furnished, the letter to Madera County as part of the personal loan transaction (which is nowhere explained in the record), the statement in the letter was correct: 41/49 had satisfied its obligation to contribute all of the utility plant under its main extension agreement with Hillview. Second, the personal loan was not recorded as a company loan at all; *see* the explanation in the preceding section. Third, Staff has offered no evidence to support its allegation that there was an effort to mislead us or the Golden Oak Bank, and our 1993 general rate case indicates just the opposite.

There is no substantial evidence in the record to convince us that the respondents "schemed" to conceal the personal loan to the Forresters, the proceeds of which were used principally to pay off Hillview's indebtedness. That debt reflected loans extended to the company by the Forresters, and by Linton apparently before he conveyed ownership to Forrester and Forrester's sister. Only the disposition of the remaining $141,546.97 is of any concern to us, and both Forrester and Peasley testified that Forrester reimbursed that sum to Hillview in 1998 in satisfaction of the loan he and Judith had received from Hillview. We infer from this succession of events and the absence of a cash transaction of this amount that Forrester and his ex-wife Judith simply retained

the $141,546.97 loaned to them by 41/49, and gave the company a note in that amount to document that portion of the loan to the company; the company recorded the entire transaction as a $350,000 loan from the Forresters, and canceled the outstanding indebtedness to them in partial satisfaction thereof.

This leaves unaccounted for only the four withdrawals from the SDWBA surcharge account made by Judith, totaling $15,541.16. Forrester became defensive when questioned at the EH about these withdrawals, and we infer that his marital difficulties with Judith were very likely involved. These funds (which are not included in the succession of loans recounted above), were withdrawn as payments to the Forresters in satisfaction of their loan to Hillview. It appears that this was improper, and there is no record that they were ever repaid to the SDWBA account.[17] If this is true, these funds must be reimbursed to the account with interest at the rate applicable to the SDWBA account at the time the withdrawals were made.

Conclusion

There is substantial evidence in the record demonstrating that the respondents engaged in conduct that, on its face, was contrary to various Commission-approved tariffs and statutes this Commission enforces. Instances of this conduct are specifically enumerated in the Findings of Fact and

[17] If the Forresters (or either of them) retained the initial $141,546.97 and the $15,541.16 as well, it appears that the latter sum should have been recorded as a loan to Forrester and Judith, and repaid with interest to the SDWBA surcharge account. If this reimbursement has not been made, the company's customers will apparently have funded these cash payments to the Forresters through withdrawals from the company's SDWBA surcharge account.

Conclusions of Law. The respondents have candidly admitted committing these acts.

Many of these compliance problems have already been redressed by previous Commission orders, including the approval of a reduced rate of return in the Hillview's 1993 general rate case as a direct consequence of its failure to seek approval of previous loans. Customers who paid "supply and storage" fees that were arguably subject to partial refund have paid lower rates as the result of the company's treatment of these fees as contributions instead of advances, and it appears that accurate reconstruction of records on the basis of which refunds potentially could be made is impossible in any event. The rate consequences to customers of the initially underreported CIAC balance were offset by the company's increased investment in plant on which it earned no return over an eight-year period during the course of this investigation.

Since 1996 the company has utilized the services of legal and accounting professionals, and as far as we are aware its compliance history has been satisfactory since that time. Staff has made no effort to amend the OII or institute a new proceeding as directed in OP 1 to bring to our attention any additional allegations of misconduct on the part of the company or its owners.

These facts indicate that although the company's conduct, particularly during the period from 1991 through 1994, was reprehensible in many respects, no harm has come to its customers, with the exception of any consequences from the loss of funds that may have been misappropriated from the SDWBA account by Judith. Moreover, in other phases of this proceeding, we saw evidence that Hillview is making conscientious efforts to finance and build sorely needed supply and treatment facilities to serve its customers.

The respondents argue that, notwithstanding any finding we make on the merits that they violated a statute or rule, we are barred by various statutes of limitations from granting any relief in the form of penalties or restitution to individual customers. We need not reach this issue in light of our determination to forgo such relief in this proceeding. Our major concern is to ensure that the company provides a full and accurate accounting to reflect our findings, and to make a rate adjustment pursuant to OP 5 of the OII if necessary.

Our order also provides that Staff may, in a new proceeding, seek to have water service provided to Hillview's customers by means other than a utility managed by Forrester if, within five years, there is a recurrence of the violations we have found here. OP 5 expressly provides for such relief in the event that it appears Forrester is unfit to manage a public utility. It does not so appear on the record before us, but we order this probationary relief as a precaution to prevent future regulatory compliance lapses.

Comments on the Proposed Decision

The proposed decision of the ALJ was mailed to the parties in accordance with Public Utilities Code Section 311(d), and opportunity for comment was provided pursuant to Rules 77.2-77.5 of the Rules of Practice and Procedure. Initial comments were timely filed by Staff. Respondents filed no initial comments, but filed reply comments on May 30, 2003. These reply comments are untimely, and are rejected.

Staff's comments basically reargue positions taken in its briefs, contend that certain pivotal facts should be construed differently and findings altered accordingly, and assert that all of the ordering paragraphs of our order are in error. Under Rule 77.3, comments must point out specific errors in a proposed decision, and may not "merely reargue positions taken in briefs. . . ." Comments

that attempt such reargument "will be accorded no weight and are not to be filed." Staff's comments do not show any factual, legal, or technical error in the proposed decision, and we therefore reject staff's requested changes.

Assignment of Proceeding

Susan P. Kennedy is the Assigned Commissioner and Victor D. Ryerson is the assigned ALJ in this proceeding.

Findings of Fact

1. The $25,000 withdrawal from Hillview's SDWBA account on January 31, 1992, was not approved by the Commission. It was, however, approved by the Department of Water Resources, and was used for utility purposes.

2. The four withdrawals from Hillview's SDWBA account on June 30, July 31, September 30, and October 30, 1993, were paid to Forrester and his ex-wife Judith, and were not approved by the Commission.

3. The respondents did not seek prior Commission approval of the $424,000 SBA loan to Hillview in 1994. Res. No. W-3833 (March 9, 1994) reflects that the Commission was by then aware of this unauthorized borrowing.

4. By July 31, 1998, Forrester paid all of the $141,546.97 owed to Hillview as partial repayment of the $350,000 the company had loaned to him and his ex-wife, Judith.

5. Hillview sought prior approval of the two CoBank loans by a draft AL filed on October 6, 1993. Res. No. F-632, issued in response to the request on November 22, 1994, reflects that the Commission was aware Hillview was in violation of Section 825 for failure to secure prior approval of Hillview's commercial debt.

6. Hillview modified certain Commission-approved service connection applications and main extension contract forms used to implement Tariff Rule 15, by inserting provisions requiring the customer to pay a nonrefundable "Supply and Storage Fee." The term, "Supply and Storage Fee" does not appear in Tariff Rule 15 or any other Commission-approved tariff that pertains to this investigation.

7. From 1982 until at least 1993, utilities were only permitted to collect fees to pay for supply and storage facilities from developers, and not from individuals, under the terms of Commission-approved tariffs.

8. Hillview collected "Supply and Storage Fees" from individual customers until 1994. The receipt of all such fees was recorded in Hillview's CIAC accounts, and the funds were used to add supply and storage facilities needed to serve the districts in which the properties for which they were paid are located.

9. The "Supply and Storage Fees" Hillview collected were not included in its rate base, and the company has not earned a return on these funds.

10. Hillview's failure to refund these fees as advances pursuant to the refund schedule in Paragraph C.2.c of Tariff Rule 15 was contrary to the express requirements of that tariff.

11. Hillview did not properly make the election to treat payments for customers as non-refundable contributions under applicable tariff rules.

12. Hillview's practice of collecting "Supply and Service Fees" until June 1994 was not provided for in Tariff Rule 15.

13. Hillview's alteration and use of Commission-approved forms used to implement Tariff Rule 15 without obtaining prior Commission authority was contrary to Paragraph A.1.a of that tariff.

14. Hillview's noncompliance with Commission-approved tariffs as described herein did not harm customers or benefit the respondents, because any fees paid by individual customers that might otherwise have been refundable were used for construction of supply and storage facilities serving their properties, and the cost of those facilities was not recorded in rate base or used in setting customers' rates.

15. In response to two data requests, Hillview furnished to Staff photocopies of completed application forms that had been altered by replacement of the bottoms of the original documents. The principal instance was a data request for a list of customer names. Production of the names in this fashion was responsive to the request, and any obliterated information was readily available to Staff.

16. There is no substantial evidence that the respondents altered any documents in an effort to mislead the Commission.

17. Hillview did not enter into main extension contracts with Longs Drugs or Vons Markets in compliance with Tariff Rule 15 when those customers arranged for service to the properties involved in this investigation.

18. There is no substantial evidence in the record that respondents diverted revenue collected expressly to repay its SDWBA loans from the special surcharge account and applied them to other purposes, including personal business use by Forrester, *except* for the withdrawals referred to in Finding of Fact 2, above, which were purportedly payments to Forrester and his ex-wife Judith in partial satisfaction of a debt owed to them by Hillview.

19. There is no substantial evidence in the record that Hillview submitted AL 53 for additional authority to expand facilities and increase indebtedness, and in it misstated the level of the special fund account due to diversion in a manner prohibited by Commission rules and orders.

20. The Forresters' assumption of a $47,900 loan to the company by Linton and cancellation of that debt as part of the 1992 loan transaction was based upon a substantiated pre-existing obligation to Linton for sums he had advanced on behalf of the company and cash he had paid to the company.

21. In the 1992 transaction, Forrester did not immediately loan $141,546.97 to the company, as reflected in the terms recorded for that loan transaction.

22. The book entry made in 1992 that included the $350,000 obligation was not properly recorded. That transaction should have been recorded as set forth in Exh. 124 under proper accounting procedure.

23. As a result of improper recording of the 1992 transaction, Hillview's CIAC was understated, and its rate base was overstated, by $141,546.97 for the 1994 test year. However, Hillview's rate base was actually understated at that time, because its recorded average plant in 1994 was higher than the test year average plant which was used to set Hillview's rates for the period from 1993 until 2001, when we granted a general rate adjustment in this proceeding.

24. In the 1993 General Rate Case, we adopted a low rate of return for Hillview because of its previous unauthorized borrowing activities.

25. The plant contributed by 41/49 pursuant to its 1992 main extension contract with Hillview was in fact installed.

26. At the time 41/49 made the $350,000 loan to the Forresters, it had already fully satisfied its obligation to contribute utility plant under its main extension contract with Hillview.

27. The $350,000 personal loan to the Forresters was not recorded as a loan to the company.

28. There is no evidence that Hillview obtained the $424,000 SBA loan in order to mislead Golden Oak Bank or the Commission.

Conclusions of Law

1. Based upon the foregoing findings, the respondents violated Section 491 prior to July 31, 1994, by conduct contrary to various provisions of Commission-approved tariffs.

2. Based upon the foregoing findings, the respondents did not violate Section 581 as alleged in the OII.

3. Based upon the foregoing findings, the respondents violated Section 825 by incurring indebtedness on behalf of Hillview without first obtaining an order of the Commission granting authority to do so.

4. Based upon the foregoing findings, the respondents did not violate Commission Rule of Practice and Procedure 1, as alleged in the OII.

5. Based upon the foregoing findings, the respondents should not be ordered to pay any fine or make any refund to individual customers. Any requirement for the respondents to pay a fine would further weaken the financial condition of the company to the detriment of its ratepayers.

6. Based upon the foregoing findings, a final reconciliation of Hillview's accounts should be prepared to explain and correct any discrepancies or irregularities identified in the findings, for the period from January 1, 1991, through July 31, 1998. If any misappropriation of funds is discovered in that reconciliation, those funds should be repaid to Hillview with interest at the rate applicable to the SDWBA account at the time of their withdrawal.

7. Based upon the foregoing findings, the respondents should be subject to a five-year period of probation to ensure that any further violation of the statutes they have been shown to have violated herein will be properly remedied. Such remedies should include consideration of providing water service to Hillview's customers by other means than a utility managed by Forrester.

FINAL ORDER

IT IS ORDERED that:

1. Within 60 days of the effective date of this order, the respondents Hillview Water Company, Inc. (Hillview) and Roger L. Forrester (Forrester), the principal shareholder and president, shall prepare and file with the Commission's Water Division a final reconciliation of Hillview's accounts for the period from January 1, 1991, to and including July 31, 1998, that fully explains all of the discrepancies and irregularities identified in the Findings of Fact. This reconciliation shall include, but shall not be limited to, a full accounting of the disposition of the withdrawals from Hillview's Safe Drinking Water Bond Act (SDWBA) account made between June 30 and October 30, 1993, by respondent Forrester or his ex-wife, Judith. If the reconciliation reveals that funds were misappropriated from any Hillview account by Forrester, or by anyone subject to his direction or supervision (with or without his consent), he shall repay all such funds to Hillview within 60 days, with interest at the rate applicable to Hillview's SDWBA account at the time the funds were withdrawn.

2. If the reconciliation required by Ordering Paragraph 1 indicates that Hillview's revenue requirement is materially inaccurate, Hillview shall file, within 60 days, an informal general rate case to properly adjust its rates. The effective date of the resulting rates shall be the date when the informal general rate case is filed.

3. The respondents shall comply with all statutes, rules, and orders administered under the jurisdiction of this Commission.

4. A new proceeding, incorporating the record of this investigation, shall be instituted if, within five years after the effective date of this Order the

Commission's Water Division shows by declaration made under penalty of perjury that the respondents, or either of them, have violated Section 491 or Section 825 of the California Public Utilities Code. Consideration may then be given to providing service to Hillview's customers by means other than a utility managed by respondent Forrester.

5. Investigation 97-07-018 is closed.

This order is effective today.

Dated _____, at San Francisco, California.